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Report on

2010 Inspection of Colabella & Company, LLP
(Headquartered in Brooklyn, New York)

Issued by the

Public Company Accounting Oversight Board

March 31, 2011

THIS IS A PUBLIC VERSION OF A PCAOB INSPECTION REPORT

**PORTIONS OF THE COMPLETE REPORT ARE OMITTED
FROM THIS DOCUMENT IN ORDER TO COMPLY WITH
SECTIONS 104(g)(2) AND 105(b)(5)(A)
OF THE SARBANES-OXLEY ACT OF 2002**

PCAOB RELEASE NO. 104-2011-098A
(Includes portions of Parts II and IV of the full report that
were not included in PCAOB Release No. 104-2011-098)



Notes Concerning this Report

1. Portions of this report may describe deficiencies or potential deficiencies in the systems, policies, procedures, practices, or conduct of the firm that is the subject of this report. The express inclusion of certain deficiencies and potential deficiencies, however, should not be construed to support any negative inference that any other aspect of the firm's systems, policies, procedures, practices, or conduct is approved or condoned by the Board or judged by the Board to comply with laws, rules, and professional standards.
2. Any references in this report to violations or potential violations of law, rules, or professional standards should be understood in the supervisory context in which this report was prepared. Any such references are not a result of an adversarial adjudicative process and do not constitute conclusive findings of fact or of violations for purposes of imposing legal liability. Similarly, any description herein of a firm's cooperation in addressing issues constructively should not be construed, and is not construed by the Board, as an admission, for purposes of potential legal liability, of any violation.
3. Board inspections encompass, among other things, whether the firm has failed to identify departures from U.S. Generally Accepted Accounting Principles ("GAAP") or Securities and Exchange Commission ("SEC" or "Commission") disclosure requirements in its audits of financial statements. This report's descriptions of any such auditing failures necessarily involve descriptions of the related GAAP or disclosure departures. The Board, however, has no authority to prescribe the form or content of an issuer's financial statements. That authority, and the authority to make binding determinations concerning an issuer's compliance with GAAP or Commission disclosure requirements, rests with the Commission. Any description, in this report, of perceived departures from GAAP or Commission disclosure requirements should not be understood as an indication that the Commission has considered or made any determination regarding these issues unless otherwise expressly stated.

2010 INSPECTION OF COLABELLA & COMPANY, LLP

In 2010, the Public Company Accounting Oversight Board ("PCAOB" or "the Board") conducted an inspection of the registered public accounting firm Colabella & Company, LLP ("the Firm"). The Board is issuing this report of that inspection in accordance with the requirements of the Sarbanes-Oxley Act of 2002 ("the Act").

The Board is making portions of the report publicly available. Specifically, the Board is releasing to the public Part I of the report and portions of Part IV of the report. Part IV of the report consists of the Firm's comments, if any, on a draft of the report.^{1/}

The Board has elsewhere described in detail its approach to making inspection-related information publicly available consistent with legal restrictions.^{2/} A substantial portion of the Board's criticisms of a firm (specifically criticisms of the firm's quality control system), and the Board's dialogue with the firm about those criticisms, occurs out of public view, unless the firm fails to make progress to the Board's satisfaction in addressing those criticisms. In addition, the Board generally does not disclose otherwise nonpublic information, learned through inspections, about the firm or its clients. Accordingly, information in those categories generally does not appear in the publicly available portion of an inspection report.

^{1/} The Board does not make public any of a firm's comments that address a nonpublic portion of the report unless a firm specifically requests otherwise. In addition, pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(b), if a firm requests, and the Board grants, confidential treatment for any of the firm's comments on a draft report, the Board does not include those comments in the final report at all. The Board routinely grants confidential treatment, if requested, for any portion of a firm's response that addresses any point in the draft that the Board omits from, or any inaccurate statement in the draft that the Board corrects in, the final report.

^{2/} See Statement Concerning the Issuance of Inspection Reports, PCAOB Release No. 104-2004-001 (August 26, 2004).

PART I

INSPECTION PROCEDURES AND CERTAIN OBSERVATIONS

Members of the Board's inspection staff ("the inspection team") conducted primary procedures for the inspection from June 28, 2010 to July 1, 2010. These procedures were tailored to the nature of the Firm, certain aspects of which the inspection team understood at the outset of the inspection to be as follows:

Number of offices	1 (Brooklyn, New York)
Ownership structure	Limited liability partnership
Number of partners	2
Number of professional staff ^{3/}	1
Number of issuer audit clients ^{4/}	1

^{3/} "Professional staff" includes all personnel of the Firm, except partners or shareholders and administrative support personnel. The number of partners and professional staff is provided here as an indication of the size of the Firm, and does not necessarily represent the number of the Firm's professionals who participate in audits of issuers or are "associated persons" (as defined in the Act) of the Firm.

^{4/} The number of issuer audit clients shown here is based on the Firm's self-reporting and the inspection team's review of certain information for inspection planning purposes. It does not reflect any Board determination concerning which, or how many, of the Firm's audit clients are "issuers" as defined in the Act. In some circumstances, a Board inspection may include a review of a firm's audit of financial statements and internal control over financial reporting ("ICFR") of an issuer that ceased to be an audit client before the inspection, and any such former clients are not included in the number shown here.

Board inspections are designed to identify and address weaknesses and deficiencies related to how a firm conducts audits.^{5/} To achieve that goal, Board inspections include reviews of certain aspects of selected audits performed by the firm and reviews of other matters related to the firm's quality control system.

In the course of reviewing aspects of selected audits, an inspection may identify ways in which a particular audit is deficient, including failures by the firm to identify, or to address appropriately, respects in which an issuer's financial statements do not present fairly the financial position, results of operations, or cash flows of the issuer in conformity with GAAP.^{6/} It is not the purpose of an inspection, however, to review all of a firm's audits or to identify every respect in which a reviewed audit is deficient. Accordingly, a Board inspection report should not be understood to provide any assurance that the firm's audits, or its issuer clients' financial statements or reporting on internal control, are free of any deficiencies not specifically described in an inspection report.

In addition, inclusion of a deficiency in an inspection report does not mean that the deficiency remained unaddressed after the inspection team brought it to the firm's attention. Under PCAOB standards, when audit deficiencies are discovered after the date of the audit report, a firm must take appropriate action to assess the importance of the deficiencies to the firm's present ability to support its previously expressed audit opinions.^{7/} Depending upon the circumstances, compliance with these standards may

^{5/} This focus on weaknesses and deficiencies necessarily carries through to reports on inspections and, accordingly, Board inspection reports are not intended to serve as balanced report cards or overall rating tools.

^{6/} When it comes to the Board's attention that an issuer's financial statements appear not to present fairly, in a material respect, the financial position, results of operations, or cash flows of the issuer in conformity with GAAP, the Board's practice is to report that information to the SEC, which has jurisdiction to determine proper accounting in issuers' financial statements.

^{7/} See AU 390, *Consideration of Omitted Procedures After the Report Date*, and AU 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report* (both included among the PCAOB's interim auditing standards, pursuant to PCAOB Rule 3200T), and PCAOB Auditing Standard No. 5, *An Audit of Internal Control Over*

require the firm to perform additional audit procedures, or to inform a client of the need for changes to its financial statements or reporting on internal control, or to take steps to prevent reliance on previously expressed audit opinions. A Board inspection does not typically include review of a firm's actions to address deficiencies identified in that inspection, but the Board expects that firms are attempting to take appropriate action, and firms frequently represent that they have taken, are taking, or will take, action. If, through subsequent inspections or other processes, the Board determines that the firm failed to take appropriate action, that failure may be grounds for a Board disciplinary sanction.

A. Review of Audit Engagement

The inspection procedures included a review of aspects of one audit performed by the Firm. The scope of this review was determined according to the Board's criteria, and the Firm was not allowed an opportunity to limit or influence the scope. This review did not identify any audit performance issues that, in the inspection team's view, resulted in the Firm failing to obtain sufficient competent evidential matter to support its opinion on the issuer's financial statements.

B. Review of Quality Control System

In addition to evaluating the quality of the audit work performed on a specific audit, the inspection included review of certain of the Firm's practices, policies, and procedures related to audit quality. This review addressed practices, policies, and procedures concerning audit performance, training, compliance with independence standards, client acceptance and retention, and the establishment of policies and procedures. Any defects in, or criticisms of, the Firm's quality control system are discussed in the nonpublic portion of this report and will remain nonpublic unless the Firm fails to address them to the Board's satisfaction within 12 months of the date of this report.

END OF PART I



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PORTIONS OF THE REST OF THIS REPORT ARE NONPUBLIC AND ARE OMITTED
FROM THIS PUBLIC DOCUMENT

PART II

* * * *

The inspection of the Firm included consideration of aspects of the Firm's system of quality control. Assessment of a firm's quality control system rests both on review of a firm's stated quality control policies and procedures and on inferences that can be drawn from respects in which a firm's system has failed to assure quality in the actual performance of engagements.^{8/} On the basis of the information that the inspection team reported, the Board has the following concerns about aspects of the Firm's quality control system.

1. Independence Procedures

The Firm's independence procedures appear not to meet the requirements of PCAOB Rule 3400T(b),^{9/} in that the Firm had not established a training program to provide reasonable assurance that professionals understand the Firm's independence policies.

2. Auditor Communications

The Firm's system of quality control appears not to provide sufficient assurance that the required auditor communications to the audit committee, or equivalent, occur and are appropriately documented. [Issuer A]

^{8/} A firm's failure to comply with the requirements of PCAOB standards when performing an audit may be an indication of a potentially significant defect in a firm's quality control system even if that failure did not result in an insufficiently supported audit opinion.

^{9/} PCAOB Rule 3400T(b) requires registered firms to comply with the quality control standards described in section 1000.08(o) of the American Institute of Certified Public Accountants SEC Practice Section Reference Manual, which in turn requires that a firm have policies and procedures in place to comply with Appendix L, section 1000.46 of that manual.

3. Monitoring and Addressing Identified Weaknesses

The Firm's system of quality control appears to lack a monitoring element sufficient to provide the Firm with reasonable assurance that the Firm's policies and procedures for engagement performance are suitably designed and effectively applied. The Firm's monitoring appears to have been deficient with respect to a previously identified weakness. In a report dated February 26, 2009, which related to an inspection of the Firm conducted in 2008, the Board noted that the Firm's system of quality control appeared not to provide sufficient assurance that the required auditor communications to the audit committee, or equivalent, occur and are appropriately documented. An appropriate approach to monitoring would have resulted in the Firm avoiding this deficiency in audits performed after they were brought to the Firm's attention, yet a similar deficiency was noted in this inspection.

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PART IV

RESPONSE OF THE FIRM TO DRAFT INSPECTION REPORT

Pursuant to section 104(f) of the Act, 15 U.S.C. § 7214(f), and PCAOB Rule 4007(a), the Firm provided a written response to a draft of this report. Pursuant to section 104(f) of the Act and PCAOB Rule 4007(b), the Firm's response, minus any portion granted confidential treatment, is attached hereto and made part of this final inspection report.^{10/}

^{10/} In any version of an inspection report that the Board makes publicly available, any portions of a firm's response that address nonpublic portions of the report are omitted. In some cases, the result may be that none of a firm's response is made publicly available.

Member: AICPA - NYSSCPA - PCPS

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managing partner

♦
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January 12, 2011

PCAOB
1666 K Street, N.W.
Washington, DC 20006
Attention: George H. Diacont

Re: Draft Report of Inspection

Dear Mr. Diacont:

This letter is in response to your letter of December 14, 2010, regarding the draft of the inspection report of our firm for the year 2010.

We are responding to three specific conclusory comments noted in part 2, "Detailed Discussion of Inspection Results". We are responding to each comment by reiterating the exact comment noted in part 2 therein and providing a "response".

1. Independence Procedures

The Firm's independence procedures appear not to meet the requirements of PCAOB Rule 3400T(b), in that the Firm had not established a training program to provide reasonable assurance that professionals understand the Firm's independence policies.

Response:

The PCAOB inspection refers to a broad based rule 3400T and does not specifically state the requirement that is not met. We submit that our firm is in full compliance with the AICPA SEC Practice Section's Requirements of Membership.

Rule 3400 T(b) refers to Interim Quality Control Standards as follows:

A registered public accounting firm, and its associated persons, shall comply with quality control standards, as described in -(a) the AICPA's Auditing Standards Board's Statements on Quality Control Standards, as in existence on April 16, 2003 (AICPA Professional Standards, QC §§ 20-40 (AICPA 2002)), to the extent not superseded or amended by the Board; and **(b) the AICPA SEC Practice Section's Requirements of Membership (d), (f)(first sentence), (l), (m), (n)(1) and (o), as in existence on April 16, 2003 (AICPA SEC Practice Section Manual § 1000.08(d), (f), (j), (m), (n)(1) and (o)), to the extent not superseded or amended by the Board.** SEC Practice Section (SECPS) - Requirements of Membership are as follows:

Section 1000.08(d) – Continuing Professional Education of Audit Firm Personnel

Ensure that all professionals in the firm residing in the United States, including CPAs and non-CPAs, participate in at least 20 hours of qualifying continuing professional education (CPE) every year and at least 120 hours every three years. Effective for CPE years beginning on or after January 1, 1995, professionals who devote at least 25% of their time to performing audit, review or other attest engagements (excluding compilations), or who have the partner/manager-level responsibility for the overall supervision or review of any such engagements, must obtain at least 40% (eight hours in any one year and 48 hours every three years) of their required CPE in subjects relating to accounting and auditing. The term accounting and auditing subjects should be broadly interpreted, and for example, include subjects relating to the business or economic environments of the entities to which the professional is assigned.

Section 1000.08(l) – Communication by Written Statement to all Professional Personnel of Firm Policies and Procedures on the Recommendation and Approval of Accounting Principles, Present and Potential Client Relationships, and the Types of Services Provided.

Communicate through a written statement to all professional firm personnel the broad principles that influence the firm's quality control and operating policies and procedures on, as a minimum, matters related to the recommendation and approval of accounting principles, present and potential client relationships, and the types of services provided, and inform professional firm personnel periodically that compliance with those principles is mandatory (Appendix H, SECPS §1000.42 is an illustration of such a statement.)

Section 1000.08(o) – Policies and Procedures to Comply with Independence Requirements

Ensure that the member firm has policies and procedures in place to comply with applicable independence requirements of the AICPA, SEC and Independence Standards Board.^{fn7}

We enclose a complete copy of our manual and a copy of the independence confirmation that we use. We submit that it is in full compliance with the requirements set out under PCAOB rule 3400T (b).

2. Auditor Communications

The Firm's system of quality control appears not to provide sufficient assurance that the required auditor communications to the audit committee, or equivalent, occur and are appropriately documented.

Response

We enclose a copy of our communications with the audit firm. The one client we have is a corporate shell and has no audit committee. In addition, we are in full compliance with CPE requirements. We have been peer reviewed with no such deficiency.

3. Monitoring and Addressing Identified Weaknesses

The Firm's system of quality control appears to lack a monitoring element sufficient to provide the Firm with reasonable assurance that the Firm's policies and procedures for engagement performance are suitably designed and effectively applied. The Firm's monitoring appears to have been deficient with respect to a previously identified weakness. In a report dated February 26, 2009, which related to an inspection of the Firm conducted in 2008, the Board noted that the Firm's system of quality control appeared not to provide sufficient assurance that the required auditor communications to the audit committee, or equivalent, occur and are appropriately documented. An appropriate approach to monitoring would have resulted in the Firm avoiding this deficiency in audits performed after they were brought to the Firm's attention, yet a similar deficiency was noted in this inspection.

Response:

The previously identified weakness was addressed. The PCAOB inspectors insisted on a rewording of our communications with the audit firm confirming our independence. We emphatically reject this deficiency as baseless.

The deficiency states “...appeared not to provide sufficient assurance that the required auditor communications to the audit committee, or equivalent, occur and are appropriately documented. This is entirely not true.

How could this be when the very correspondence they wish altered was in compliance with the 2008 comment?

We trust that the comments will be removed. Thank you for your cooperation in this matter.

Very truly yours,

A handwritten signature in black ink, appearing to read 'P. Colabella', with a long, sweeping horizontal flourish extending to the right.

Patrick R. Colabella
Managing Partner